

**Internal Revenue Service**

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402.09-00  
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Department of the Treasury

**199947041**

Washington, DC 20224

Person to Contact

Telephone Number:

Refer Reply to: OP:E:EP:T:4

Date:

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Attn:

Legend:

Plan X =

Company A =

Dear

This letter is in response to your request for a private letter ruling dated December 14, 1998, as supplemented by a letter dated April 30, 1999, submitted on your behalf by your authorized representative, regarding the federal income tax treatment of certain distributions to participants in Plan X.

Plan X is an employee stock ownership plan which is intended to qualify under sections 401(a) and 4975(e)(7) of the Internal Revenue Code ("Code"). The related trust is exempt from income taxation under section 501(a) of the Code. Plan X, including the related trust agreement, was last amended and restated on September 10, 1997. Plan X received its most recent favorable determination letter on March 26, 1998.

Company A maintains Plan X as a C corporation as defined in section 1361(a)(2) of the Code. Neither Company A nor any subsidiary of Company A maintains any other tax-qualified plan. Every Plan X participant is an employee of Company A, including any employee who works at a subsidiary of Company A.

Section 6.01 of Plan X provides that a participant can receive a distribution of his or her Plan benefits in the event of his or her retirement or other termination from employment with Company A. Under Section 6.03(B) of Plan X, as amended in September 1997, a participant who has not retired or otherwise separated from employment can elect a distribution of all of his or her Plan benefits at any time on or after he or she attains age 68-1/2 and has 10 years of vesting service. In both instances, the terms of Plan X provide a single sum payment.

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Pursuant to Section 9.11(A) of Plan X, shares of Company A common voting stock and/or shares of Company A common nonvoting stock are allocated to a participant's Plan account. The common voting stock of Company A is a "qualifying employer security" as defined by Code sections 4975(e)(8) and 409(l)(2). This voting stock and Company A's common nonvoting stock are "securities of the employer corporation" as defined by Code section 402(e)(4)(E)(ii). Under Section 10.08 of Plan X, either or both classes of stock may be distributed to a participant in an in-service distribution or in the event of a participant's separation from service with Company A.

Pursuant to Section 6.03(B) of Plan X, a Plan participant with 10 years of vesting service who has attained at least age 68-1/2 can elect to receive an in-service distribution of his or her entire Plan benefits in one payment for which the Plan trustee will make a single payment representing the participant's entire account balance. Prior to receiving this in-service distribution, the Plan participant will have received on a regular quarterly basis any cash dividend payable on Company A common voting stock allocated to the participant's Plan account. These dividend payments are made by Company A directly to the Plan participant, pursuant to Section 10.08 of Plan X and section 404(k)(2)(A)(i) of the Code.

Your authorized representative has stated that a specific participant intends to elect an in-service distribution of his or her entire Plan benefits under Section 6.03(B) of Plan X during the 1999 calendar year. Also, it has been represented that at least one participant who has separated from service with Company A during the 1999 calendar year received a distribution of his or her entire account balance, having already received dividend distributions in prior years pursuant to section 404(k)(2)(A)(i) of the Code.

Based on the above facts and representations, you have requested the following two rulings:

1. That the payment of an active participant's entire account balance in one taxable year, on or after he attains age 68-1/2 and has ten years of vesting service, constitutes a lump sum distribution under Code sections 402(d)(4)(A) and 402(e)(4)(D) even though in years prior to this payment, including years after the participant attained age 59-1/2, the participant received dividend distributions from the Plan pursuant to Code section 404(k)(2)(A)(i).
2. That the payment of a participant's entire account balance in one taxable year after he separates from service with Company A constitutes a lump sum distribution under Code sections 402(d)(4)(A) and 402(e)(4)(D) even though in years prior to this payment, including years after his separation from service and attainment of age 59-1/2, the participant received dividend distributions from the Plan pursuant to Code section 404(k)(2)(A)(i).

Section 402(d)(4)(A) of the Code (effective for taxable years beginning before January 1, 2000) provides that for purposes of this section and section 403, the term "lump sum distribution" means, in pertinent part, the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient under clause (ii), after the employee attains age 59-1/2, or under clause (iii), on account of the employee's separation from service.

Section 402(e)(4)(B) of the Code provides, in pertinent part, that for purposes of subsection (a) and section 72, in the case of any lump sum distribution which includes securities of the employer corporation, there shall be excluded from gross income the net unrealized appreciation attributable to that part of the distribution which consists of securities of the employer corporation.

Section 402(e)(4)(D) of the Code (effective for taxable years beginning before January 1, 2000) provides that for purposes of this paragraph, the term "lump sum distribution" has the meaning given such term by subsection (d)(4)(A) (without regard to subsection (d)(4)(F)).

Section 402(e)(4)(D) of the Code (effective for taxable years beginning after December 31, 1999) provides that for purposes of this paragraph, the term "lump sum distribution" means, in pertinent part, the distribution or payment within one taxable year of the recipient of the balance to the credit of an employee which becomes payable to the recipient, under subparagraph (D)(i)(II), after the employee attains age 59-1/2, or under subparagraph (D)(i)(III), on account of the employee's separation from service.

Section 402(e)(4)(E)(ii) of the Code provides that the term "securities of the employer corporation" includes securities of a parent or subsidiary corporation (as defined in subsections (e) and (f) of section 424) of the employer corporation.

Section 404(k)(2)(A)(i) of the Code provides a deduction to a C Corporation for any cash dividend paid during a taxable year with respect to its stock held in an employee stock ownership plan which it maintains, if the dividend is paid directly to the plan participants, or their beneficiaries. Similarly, section 404(k)(2)(A)(ii) of the Code provides a deduction if the cash dividend is paid to the employee stock ownership plan and distributed to participants, or their beneficiaries, within 90 days after the close of the plan year in which the dividend is paid. In both instances, the deduction is limited to dividends paid on "employer securities" as defined under sections 409 (l) and 404(k)(6)(A) of the Code.

Section 1.404(k)-IT, Q & A-3, of the Temporary Regulations provides that dividends paid in cash directly to plan participants by the corporation and dividends paid to the plan and then distributed in cash to plan participants under section 404(k) of the Code are generally treated as plan distributions for the purposes of sections 72, 401 and 402 of the Code.

Pursuant to section 10.08 of Plan X, dividends on Company A's common voting stock held in Plan X are paid by Company A directly to participants in Plan X as provided under section 404(k)(2)(A)(i) of the Code. Such dividends are not treated as part of the balance to the credit of an employee for purposes of determining a lump sum distribution under section 402(d)(4)(A) of the Code (effective for "pre-2000" taxable years) and section 402(e)(4)(D) of the Code (effective for "pre-2000" taxable years and "post-1999" taxable years). Thus, such distribution does not prevent a subsequent distribution of the balance to the credit of an employee from being a lump sum distribution.

Accordingly, with respect to your first ruling request, we conclude that the payment of an active participant's entire account balance in one taxable year, on or after the participant attains age 68-1/2 and has ten years of vesting service, constitutes a lump sum distribution under Code sections 402(d)(4)(A) and 402(e)(4)(D) even though in years prior to this payment, including years after the participant attained age 59-1/2, the participant received dividend distributions pursuant to Code section 404(k)(2)(A)(i) that are treated as distributions from Plan X.

With respect to your second ruling request, we conclude that the payment of a participant's entire account balance in one taxable year after the participant separates from service with Company A constitutes a lump sum distribution under Code sections 402(d)(4)(A) and 402(e)(4)(D) even though in years prior to this payment, including years after the participant's separation from service and attainment of age 59-1/2, the participant received dividend distributions pursuant to Code section 404(k)(2)(A)(i) that are treated as distributions from Plan X.

The above rulings are based on the assumption that Plan X is qualified under sections 401(a) and 4975(e)(7) of the Code and its related trust exempt from tax under section 501(a) of the Code at all relevant times.

Please be aware that the taxable portion of an "eligible rollover distribution" described in section 402(c)(4) of the Code is subject to the 20-percent withholding requirement under section 3405(c) of the Code.

This letter ruling is directed only to the taxpayer who requested it. Section 6110(k)(3) of the Code provides that it may not be used or cited by others as precedent.

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The original of this letter ruling has been sent to your authorized representative pursuant to a power of attorney on file with this office.

Sincerely yours,

*John G. Riddle, Jr.*

John G. Riddle, Jr.  
Chief, Employee Plans  
Technical Branch 4

Enclosures:

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Notice 437

cc:

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